The Issue

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Making financial management assessments quicker, more reliable and easier to deploy

Start the game off right by scripting your opening plays

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Bill Walsh, pro football Hall of Fame coach, mastered the art of the opening sequence of offensive plays in a football game. Walsh believed that, "your ability to think concisely and make good judgments is much easier on Thursday night than during the heat of the game". This philosophy, of a deliberate plan of attack, offers great value in financial management assessments.

According to Walsh, the reasons for scripting the opening plays of a game were:

1. **Establish formations.** Walsh typically used different formations to see what the opponent might be doing defensively early in a game.
2. **Base offense.** The openers were great opportunities to see what the opponent was going to do to try to stop his base offensive plays.
3. **Set up certain things.** If there is a play to be used later in the game, Walsh believed in setting it up early.
4. **Specials.** Walsh included in the openers a play designed to quickly score, to produce immediate substantial results.
5. **Establish sequencer.** Establishing the sequence for success in the openers allowed for spontaneity during the latter stages.

A scripted opening set of actions greatly accelerates financial management assessment and can then be followed by fine tuning as new facts are uncovered. I have used scripted openings very effectively with a wide range of clients.

For those that have not used scripted financial assessments to better understand the client's needs and map out the steps to accomplish desired (or sometimes required) actions, assessments are judgments made by subject matter experts that are grounded in agreed upon facts. While language may differ slightly, the basic structure is Facts and Findings. In my assessments, I usually include Recommendations based on the Findings.

Scripted openers for financial assessment

The reasons for scripting opening financial assessments are:

1. **Establish formations.** I look to see how the company is currently structured and organized. Typically, this begins with a review of legal and tax entity structure, organizational structure, planning, recordkeeping and reporting and any structural wrinkles that the client may have added. I also try to mix in conversations with outside advisor groups including legal, tax and audit.
2. **Base Offense.** I look to test and identify what limitations or strengths, temporary or otherwise, that are going to affect the planning process. Typically, this script includes a review of financial reports, specific department resumes and job descriptions as well as system(s) functionality and configuration. It also includes a conversation with the owners to identify their business goals, operational, managerial and planning roles.
3. **Set up certain things.** If there is an unnecessary constraint that will affect planning, I typically set it up early for resolution.
4. **Specials.** I always make it a point to review policies and practices that, if improved, would significantly reduce costs or significantly increase scalability. In short, score early!
5. **Establish Sequencer.** Designing and prioritizing the recommendations allows management to quickly and effectively move to deployment and adjust to new challenges.

Flow of the game adjustments for financial assessments

The rationale for adjustments as information is garnered from the scripted openers is that practicing CFOs who possess years of ***subject matter*** training and ***relevant industry and/or situational*** experience are uniquely qualified to:

- Quickly and reliably adapt to the Facts and Findings, as discovered, with Recommendations that are deployable
- Quickly and reliably develop the specific actions to deploy the plans to achieve specific recommendations oftentimes with budgets and timelines
- Quickly and reliably develop the understanding and confidence of the management and staff in the deployment plan

Case Studies

Below are two shorter client financial assessment case studies that illustrate using a scripted assessment, conducted by a CFO with relevant industry and/or situational experience, to quickly produce grounded recommendations and an effective roadmap for deployment.

Software as a Service (SaaS) Company

The first example of using a scripted assessment is for a $3.0m venture backed SaaS company planning for high growth. The company had an international footprint with engineering and customer support in India, sales teams in Europe and the U.S. with the executive team in the U.S.

A financial management assessment was rapidly completed after evaluating the company's structure and organization, interviewing outside advisors, and assessing competitive advantages, challenges and special constraints, to develop grounded recommendations designed to support the unique needs of a rapidly growing SaaS company.

RECOMMENDATIONS (ROAD MAP)

1. Redesign Financial Management Reports to conform to GAAP and management reporting standards for SaaS companies retroactively to the previous year.
2. Design Unearned Revenue database to receive customer contracts data from Salesforce CRM to reliably produce monthly recurring subscription and customer support income calculations by product and region including end of month journal entries.
3. Design dashboards and KPIs for company that would conform to SaaS based companies including policies, procedures and training to reliably capture and report.
4. Develop accounting practices in the India and UK subsidiaries to meet obligation of investors to produce audited consolidated financial statements.
5. Develop a simple transfer pricing policy within the above consolidation process to avoid tax penalties and to meet tax regulations/standards.
6. Design and prepare Annual Operating Plan for current year to provide plan to actual reporting to above referenced financial management reports.
7. Develop and program an assumptions page that enables rapid extension of four additional years to the Annual Operating Plan to complete a 5-year plan.

FINDINGS (SELECTED)

1. The company has organized its sales, contracts data and accounting across SalesForce and QuickBooks. This configuration meets the market standards for companies of its size and growth opportunities. Furthermore, the fact that the data in SalesForce has been largely cleaned opens up the possibility that the data can form the source for end of month calculation of the currently missing Unearned Revenue calculations in an efficient and effective manner. Lastly, the process can be essentially automated in QuickBooks until a more expensive solution that will better scale with growth becomes practical.
2. While the systems decisions meet market standards, the recordkeeping and reporting policies do not meet those standards. Financial statements are not conformed to GAAP and would not pass an audit. Unearned subscription revenue is the obvious example for a SaaS company as it results in inaccurate revenues, gross margins and net profits. It also results in an increasingly overstated taxable income as the company grows. The company also enters the expenses from the Indian subsidiary directly into the parent records without eliminating transactions between the companies. This departure from

GAAP produces cascading problems (see comments in tax reporting below). In addition, the financial statements are not conformed to management reporting standards for SaaS companies. While there is great latitude in management reporting standards, current reporting is unable to provide fundamental measurements of Total Revenue, Gross Margin, Cost of Sales & Marketing and Net Income from Operations let alone critical performance measurements associated with this business model. Lastly, the filed tax returns overstated expenses due to the lack of proper consolidating accounting practices. While there is some further investigation required, the company needs to create a simple transfer pricing policy to avoid significant penalties.

3. There are a couple of best methods that allow easy scaling by keeping much of the sales detail outside the general ledger to reduce administration costs particularly when accounting resources are limited.
4. The company does not have an Annual Operating Plan (aka Budget enhanced with SaaS performance metrics) or a five-year plan. In addition to a fundamental internal control, the annual plan is a valuable a communication tool. It is also a prerequisite to the proper pricing of stock options in their newly constituted stock option plan.

Small Business Company

The second example of using a scripted assessment is for a traditional small business, an engineering services company with $4.8m revenues that was struggling with understanding the relationship between profitability and cash flow. While this confusion was tolerated when the company entered into “time and expense” contracts with regular billing cycles, it was not when entering into larger “fixed” contracts with milestone billing cycles particularly when a majority are with governmental clients.

With a slightly different script, an industry experienced consulting CFO completed evaluating the company’s structure, organization, interviewing outside advisors, and assessing competitive advantages, challenges and special constraints, to develop unique recommendations for a rapidly changing company.

RECOMMENDATIONS (ROAD MAP):

1. Produce fully accrued financial statements for each quarter to document the profitable operations including establishing standards for billing and entering accounts payable invoices within an agreed upon days of receipt.
2. Develop sources of working capital for anticipated increase in Accounts Receivable and Unbilled Time including increase existing accounts receivable line of credit to $500,000; investigate personal line of credit up to $250,000 to finance increase in unbilled time.
3. Develop the Personnel Assumptions worksheet only, for the time being, so that owner/CEO has billable hours, average bill rate and pay rate targets to plan, monitor and control professional staff productivity and profitability in the short term until time allows completion of a comprehensive company-wide financial plan.
4. Design and train controller to produce an Hours/Dollars Weekly Flash Report by billing professional, by task, by project and by category utilizing burdened pay-rates.
5. Work with controller to integrate job costs, such as subcontractors, into the current job cost database that is only assigning professional staff actual payroll.

6. Redesign and reorganize the current QuickBooks reporting from simple alphabetic listing of income and expenses into a departmental approach (e.g. professional services, customer support, sales & marketing, general & administrative) so as to produce crucial measurements of gross margin, contribution margin and net income from operations.
7. Create tax reporting practices between company and tax accountant that clearly reconcile profitable accrued financial results to unprofitable "cash basis" tax returns to support above referenced financing requirements.
8. Work with controller to develop analytical practices to reconcile and ultimately integrate job cost reporting into the monthly financial statements;

FINDINGS (SELECTED)

1. The company is creating a "perfect storm" by increasing working capital requirements and yet not producing regular financial statements that document its profitable operations and open up the possibility of external sources of debt capital.
2. The current QuickBooks/Intuit configuration will not allow effective job costing. Pending closer review of the proprietary time reporting SQL database, it may be that we could more quickly resolve the job costing requirements of the company in the SQL database where the controller seems to have a good grasp of the operations (categories, projects and tasks) and a thorough understanding of the tool (e.g. he will have the access and understanding of the SQL solution). With that said, my concern was whether the SQL can take care of the concerns of the operations manager even if could be designed to take care of the accounting concerns.
3. The current QuickBooks organization is ill-designed for the challenges facing the company. Setting aside the job costing discussed above, the fact that we can't produce meaningful financial statements is the result of an ineffective accounting practice. As an example, the company has no revenue recognition policy. Thus, revenue is recognized when billed. While this may have resulted in arguably immaterial errors for an $800,000 annual revenue company working on smaller "time and expense" type contracts, it creates very material errors for a $4.8M revenue company working on larger "fixed" type contracts. Our year-end financial statements report a $250k loss as a result of unbilled professional work during October, November and December. Accounting policy would have us inventory the work in process for that Q4 unbilled time. Without inventorying "Unbilled Time", the company will report unprofitable operations. Management is unable to determine profitability or even if the company is profitable. It also makes getting bank financing impossible.

SUMMARY

The scripted opening assessments performed by a subject matter expert produce grounded recommendations that are set and ready for immediate implementation. They are executable and prioritized road maps based on industry-specific financial executive deliberation and conversations with management, relevant staff and outside advisors. In each case, we have developed recommendations to immediately, dramatically and effectively move these companies forward

The use of scripted openers is a proven powerful aid to quicker and more affordably deployed financial management assessments for any company regardless of industry, size or situation.

I welcome your comments and thoughts, please contact me to continue the dialogue.

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